Energy Demand in the 21st Century: Are Congress and the Executive Branch Meeting the Challenge?

Statement of

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Good afternoon, Mr. Chairman and members of the Subcommittee on Energy and Resources of the House Committee on Government Reform. I am Paul R. Portney, President of Resources for the Future (RFF), a 53 year-old research organization (or "think tank") located here in Washington, DC, that specializes in energy, environmental and natural resource issues. RFF is avowedly independent and non-partisan, and it shares the results of its economic and policy analyses with members of both parties in the executive and legislative branches of government, as well as with environmental and business advocates, academics, members of the press and interested citizens. My comments today represent my own views, it should be noted, and not those of RFF, which takes no institutional position on legislative or regulatory matters.

I am pleased to be with you here today and honored to be part of such a distinguished panel. Moreover, I commend you for asking whether Congress is focusing on the most important energy questions confronting the United States and whether the federal government agencies are taking the right actions to deal with 21st century challenges and needs. In my experience, it is unusual for a congressional committee or subcommittee to step back away from the legislative fray and look at such big-picture questions. I hope other chairmen will follow your lead.

Let me plunge directly in and speak to the question you have asked us all to address: Is Congress focusing on the key energy issues facing the United States? My blunt answer is that you are, though not with the sense of urgency I believe these issues require nor, generally, in the spirit most likely to produce effective solutions.

Key Energy Issues

The most important energy issue the United States currently faces relates to the growing amount of oil we are consuming and the ever-growing fraction of it—nearly 60 percent now--that comes from other countries. With oil prices at $50 a barrel, the United States sends nearly $600 million *each day*, (a rate of $220 billion each year) out of our country to foreign sources—often to state-owned oil companies, including some in countries that are hostile to us. A $220 billion "oil bill" would account for more than a third of the greater than $600 billion annual trade deficit we currently run, a deficit that has put downward pressure on the dollar, making imported goods more expensive for Americans and threatening much higher interest rates.

Our appetite for oil has at least two consequences of concern. First, the more oil we consume in the United States (whether produced domestically or internationally), the greater is our economic vulnerability to increases in oil prices and, perhaps more importantly, to possible significant interruptions in world oil supplies (such as might be associated with a successful terrorist attack on oil production or shipping facilities in Saudi Arabia, say).

The recessions of 1974, 1980-81, 1991 and 2002 were each preceded by a run-up in world oil prices. While it is simplistic to assign all the blame for the former to the latter, there is little doubt that oil price increases act as a tax on the economy and slow its growth. *Note that this would be the case even if we produced domestically all of the oil we use.* That oil would be priced in world markets, so even if it made sense to pursue import independence, which it does not, we would still be vulnerable to oil price shocks,

whether naturally occurring (due to cold winters, for instance, which increase demand for home heating oil) or to deliberate actions (boycotts or terrorist activities).

My second point is more controversial, but you have invited me here for my advice on the congressional energy agenda, so I intend to say what I think you should hear. Another consequence of our steadily growing oil consumption is increasing atmospheric concentrations of carbon dioxide, the most significant greenhouse gas. The United States accounts for slightly less than a quarter of global annual carbon dioxide emissions, and petroleum used for personal transportation alone accounts for about 14 percent of the U.S. total. This means that the passenger cars, minivans, pickup trucks and SUVs that take us to and from work and play here in the United States account for about one out of every thirty tons of carbon dioxide emitted everywhere in the world each year.

Though I believe President Bush was right to reject the overly ambitious targets and timetables in the Kyoto Protocol, the risks of climate change demand a much more urgent response than we have seen so far. One place to begin is by improving the fuel economy of the new-vehicle fleet in the United States, especially in view of the fact that average fuel economy has declined steadily since 1986.

Whether it is a renewed and hopefully more enlightened debate on the future of Corporate Average Fuel Economy standards or a serious discussion of measures to increase the price of gasoline through gradual increases in the federal excise tax on gasoline (a better approach to stimulate fuel economy improvements, in my view), Congress needs to address this issue immediately. As painful as these debates might be, it is far better to deal with these questions now than in the midst of a serious interruption in crude oil availability.

Congress also needs to pay more attention to another hydrocarbon—natural gas. I will say less about this because both Mr. Caruso and Mr. Wells know more about this energy source than I do, and may intend to address it themselves. What I will say is that the market for natural gas seems to be evolving in the direction of that for petroleum—i.e., toward a global market in which natural gas is transported long distances in liquefied form from places where it can be produced relatively inexpensively to places where it is in great demand. Since natural gas tends to be found in many of the same places where petroleum is abundant (e.g., the Middle East), this raises the specter of a possible future "ONGEC," an Organization of Natural Gas Exporting Countries that would have the same ability to curtail supplies, and hence drive prices up, as OPEC has in the petroleum market. Given the popularity of natural gas for residential and commercial heating, as an essential feedstock for chemical and other industrial production, and (until lately, at least) for use in turbines used to generate electricity, the possibility of an eventual global natural gas cartel is something worthy of congressional attention.

To be sure, Congress has taken steps to facilitate the construction of a pipeline to bring natural gas from Alaska to the lower 48 states. But more must be done. For instance, environmental concerns have made it difficult to open up new areas for natural gas exploration and production, both on shore and on the Outer Continental Shelf. While these concerns are quite legitimate, it behooves us to ask whether new drilling and other technologies—such as those that might be used to produce natural gas on the Outer-Continental Shelf—have developed to the point where prohibitions on exploration and production ought to be revisited.

One alternative to domestic production, of course, is the importation of natural gas in liquefied form. Ramping up LNG imports, however, will require the expansion of the four existing terminals, as well as the construction of new ones. Yet (perfectly understandable) local opposition to new terminals has stymied progress on their development. If we want to make greater use of clean-burning natural gas, however, it has to come from somewhere. One thing to which Congress should give greater consideration is ways to provide compensating benefits to localities in which natural gas (and other energy sources) is either produced (on-shore in the intermountain west, for instance, or off-shore on the OCS) or imported (LNG terminals). These inducements might take the form of new government facilities that create local jobs, preferential energy prices for those living in the vicinity of wells or LNG terminals, or favorable tax treatment. If sufficient inducements cannot be created, federal preemption in the siting of energy facilities may have to be considered.

There is another aspect of energy policymaking that Congress might usefully consider: the way the federal government is organized to conduct such policy. I co-authored a paper several years ago with my then-colleague Howard Gruenspecht. We noted then that the Department of Energy (which people assume is the focal point for energy policy making in the Executive Branch) actually has very few "levers" with which to influence the types of energy we use in the United states, how and where these energy forms are used and how the energy mix should change over time.

Truth be told, the Federal Energy Regulatory Commission, the Nuclear Regulatory Commission, the Minerals Management Service, the National Highway Traffic Safety Administration and especially the Environmental Protection Agency all

have a much greater influence on energy use than does the Department of Energy. After all, one or another of these agencies make decisions that effectively determine what fuels will be used to generate electricity in the United States, what fuel economy targets the new light-duty truck fleet has to meet, what "recipes" must be used for gasoline sold in the metropolitan areas around the country, and where oil and natural gas can be produced—among other things.

It probably makes little sense to recommend a substantial reorganization of the federal government for the purposes of improved energy policymaking at a time when we are still trying to "digest" the Department of Homeland Security. But better coordination of the various actions of the Department of Energy and the five agencies mentioned immediately above—possibly through a strong and permanent Cabinet Council on Energy—would be a step in the right direction.

There are a host of other energy issues on which I would like to see Congress focus more attention. One is better internalizing the environmental "externalities" (adverse effects) associated both with fossil fuels and other forms of energy, preferably through such things as taxes on carbon or other pollutant emissions, or cap-and-trade programs. Another is working to eliminate subsidies that both distort energy decisionmaking and also cost the treasury much-needed tax receipts. A third is an expansion and rationalization of this country's energy R&D programs.

It bears brief mention that taxes on carbon dioxide or other pollutant emissions, or a cap-and-trade system in which at least some of the pollution allowances are auctioned off by the government, would not only improve the environment but also raise revenues that can be used for deficit reduction. They would also advance the cause of non-

polluting fuels such as renewables and nuclear power (though these, too, have externalities that would have to be accounted for).

Thank you very much, Mr. Chairman and Subcommittee members. That concludes my written statement and I would be happy to answer any questions you might have.